in the case of a life insurance company is limited to depletion (and depreciation) sustained on the property used, and to the extent used, for the purpose of producing the income specified in section 804(b). See section 611 and §1.611–5 for special rules relating to the depreciation of improvements in the case of mines, oil and gas wells, other natural deposits, and timber.

(6) *Trade or business deductions.* (i) Under section 804(c)(5), the deductions allowed by subtitle A of the Code (without regard to this part) which are attributable to any trade or business (other than an insurance business) carried on by the life insurance company, or by a partnership of which the life insurance company is a partner are, subject to the limitations in subdivisions (ii), (iii), and (iv) of this subparagraph, allowable as deductions from the gross investment income of a life insurance company in determining its investment yield. Such deductions are allowable, however, only to the extent that they are attributable to the production of income which is included in the life insurance company's gross investment income by reason of section 804(b)(3). However, since any interest, dividends, rents, and royalties received by any trade or business (other than an insurance business) carried on by the life insurance company, or by a partnership of which the life insurance company is a partner, is included in the life insurance company's gross investment income by reason of section 804(b)(1) and paragraph (b) of §1.804–3, any expenses fairly chargeable against the production of such income may be deductible under section 804(c) (1), (2), (3), or (4). The allowable deductions may exceed the gross income from such business.

(ii) In computing the deductions under section 804(c)(5), there shall be excluded losses:

(*a*) From (or considered as from) sales or exchanges of capital assets,

(*b*) From sales or exchanges of property used in the trade or business (as defined in section 1231(b)), and

(*c*) From the compulsory or involuntary conversion (as a result of destruction, in whole or in part, theft or seizure, or an exercise of the power of requisition or condemnation or the threat or imminence thereof) of property used in the trade or business (as so defined).

(iii) Any item, to the extent attributable to the carrying on of the insurance business, shall not be taken into account. For example, if a life insurance company operates a radio station primarily to advertise its own insurance services, a portion of the expenses of the radio station shall not be allowed as a deduction. The portion disallowed shall be an amount which bears the same ratio to the total expenses of the station as the value of advertising furnished to the insurance company bears to the total value of services rendered by the station.

(iv) The deduction for net operating losses provided in section 172, and the special deductions for corporations provided in part VIII, subchapter B, chapter 1 of the Code, shall not be allowed.

[T.D. 6513, 25 FR 12662, Dec. 10, 1960]

§ 1.806–1 Adjustment for certain reserves.

(a) For taxable years beginning after December 31, 1953, but before January 1, 1955, and ending after August 16, 1954, a life insurance company writing contracts other than life insurance or annuity contracts (either separately or combined with noncancellable health and accident insurance contracts) must add to its life insurance company taxable income (as a factor in determining 1954 adjusted taxable income) an amount equal to eight times the amount of the adjustment for certain reserves provided in paragraph (b) of this section.

(b) The adjustment for certain reserves referred to in paragraph (a) of this section shall be an amount equal to 3 1/4 percent of the mean of the unearned premiums and unpaid losses at the beginning and end of the taxable year on such other contracts as are not included in life insurance reserves. If such unearned premiums, however, are less than 25 percent of the net premiums written during the taxable year on such other contracts, then the adjustment shall be 3 1/4 percent of 25 percent of the net premiums written during the taxable year on such other contracts plus 3 1/4 percent of the mean of the unpaid losses at the beginning and end of the taxable year on such other contracts. As used in this section, the term ''unearned premiums'' has the same meaning as in section 832(b)(4) and § 1.832–1.

§ 1.806–2 Taxable years affected.

Section 1.806–1 is applicable only to taxable years beginning after December 31, 1953, and before January 1, 1955, and all references to sections of part I, subchapter L, chapter 1 of the Code are to the Internal Revenue Code of 1954, before amendments. Sections 1.806–3 and 1.806–4 are applicable only to taxable years beginning after December 31, 1957, and all references to sections of part I, subchapter L, chapter 1 of the Code are to the Internal Revenue Code of 1954, as amended by the Life Insurance Company Income Tax Act of 1959 (73 Stat. 112).

[T.D. 6513, 25 FR 12668, Dec. 10, 1960]

§ 1.806–3 Certain changes in reserves and assets.

(a) *In general.* For purposes of part I, subchapter L, chapter 1 of the Code, section 806(a) provides that if there is a change in life insurance reserves (as defined in section 801(b)), during the taxable year, which is attributable to the transfer between the taxpayer and another person of liabilities under contracts taken into account in computing such life insurance reserves, then the means of such reserves, and the mean of the assets, shall be appropriately adjusted to reflect the amounts involved in such transfer. For example, the adjustments required under section 806(a) are applicable to transfers in which one life insurance company purchases or acquires a part or all of the business of another life insurance company under an arrangement whereby the purchaser or transferee becomes solely liable on the contracts transferred. This provision shall apply in the case of assumption reinsurance but not in the case of indemnity reinsurance or reinsurance ceded. Thus, no adjustments shall be required under section 806(a) when, in the ordinary course of business, an indemnity reinsurance contract is entered into with another company (on a yearly renewable term basis, on a coinsurance basis, or otherwise) whereby there is a sharing of risks under one or more individual contracts. It will be necessary for each life insurance company participating in a transfer described in section 806(a) to make the adjustments required by such section. Such adjustments shall be made without regard to whether or not the transferor of the liabilities was the original insurer.

(b) *Manner in which adjustments shall be made*—(1) *Daily basis.* The means of the life insurance reserves, and the mean of the assets, shall be appropriately adjusted, on a daily basis, to reflect the amounts involved in a transfer described in section 806(a) and paragraph (a) of this section. The transferor and the transferee shall be treated as having held such life insurance reserves and assets for a fraction of the year in which the transfer occurs.

(2) *Determination of period held.* In determining the fraction which represents the fractional year that such reserves and assets were held, the numerator shall be the number of days during the taxable year which such reserves and assets were actually held, and the denominator shall be the number of days in the calendar year of the transfer. In computing the period held for purposes of the numerator, the day on which such reserves and assets are transferred is included by the transferor and excluded by the transferee.

(3) *Adjustments to the means of life insurance reserves and assets not transferred.* All life insurance reserves and assets transferred during the taxable year, within the meaning of section 806(a), shall be excluded from the beginning and end of the taxable year balances of the transferor and transferee, respectively. The amount of assets to be excluded from the beginning of the taxable year balance of the transferor shall be an amount equal to the value of such reserves at the beginning of the taxable year. The amount of assets to be excluded from the end of the taxable year balance of the transferee shall be an amount equal to the value of such reserves at the end of the taxable year. The means of the life insurance reserves and assets not so transferred shall be determined in the ordinary manner, that is, the arithmetic means. There shall be added to